SUPREME COURT OF THE UNITED STATES.

No. 236.—October Term, 1921.

Union Trust Company of San Francisco and Albert Lachman, as Executors of the last will and testament of Henriette S. Lachman, deceased, Plaintiffs in Error, *vs.* Justus S. Wardell, United States Collector of Internal Revenue for the First District of California, and John L. Flynn, United States Collector of Internal Revenue for the First District of California.	In Error to the District Court of the United States for the Northern District of California.

[May 1, 1922.]

Mr. Justice McKenna delivered the opinion of the Court.

This case was argued at the same time and submitted with No. 200, *Shwab* v. *Doyle*, just decided. It involves, as that case did, the Estate Tax Act of September 8, 1916, and its different facts illustrate and aid the principle upon which that case was decided.

Plaintiffs in error are executors of the last will and testament of Henriette S. Lachman, deceased. They were also parties to a trust deed made by her during her lifetime. They sued defendant in error Wardell, he then being United States Collector of Internal Revenue for the First District of California to recover the sum of $4,545.50 that being the amount of a tax assessed against the estate of Henriette S. Lachman, upon the value of 4,985 shares of stock transferred in trust by Henriette S. Lachman to trustees upon the assumption that the Act of Congress of September 8, 1916 was applicable to the trust.

The following is a summary of the facts stated narratively. On May 31, 1901, Henriette S. Lachman was the owner of 7,475 shares of the capital stock of the S. & H. Lachman Estate, a cor-

poration. On that date she executed and delivered to Albert Lachman and Henry Lachman, her sons, the following instrument:

"Almeda, Cal., May 31, 1901,

"To Albert Lachman and Henry Lachman, my sons:

"This is to certify that I have delivered to you seven thousand four hundred and seventy-five (7,475) shares of the capital stock of the S. & H. Lachman Estate, represented by certificates numbers eleven (11), twelve (12) and thirteen (13) respectively, however, upon the following trust:

"To pay to me during my lifetime, all the income earned and derived therefrom, and, upon my death, to deliver two thousand four hundred and ninety (2,490) shares, respectively by certificates number eleven (11) unto Henry Lachman, thenceforth for his absolute property; two thousand four hundred and ninety-five (2,495) shares, represented by certificate number thirteen (13) unto Albert Lachman, thenceforth for his absolute property; and yourselves, to-wit, Albert Lachman and Henry Lachman, to hold two thousand four hundred and ninety (2,490) shares, represented by certificate number twelve (12) upon my death, in trust paying the income derived therefrom unto my daughter, Rebecca, wife of Leo Metzer, and upon the death of my said daughter, the income and earnings derived from said two thousand four hundred and ninety (2,490) shares shall be held, or expended, by you, according to your judgment, for the benefit of my grandchildren, the children of my said daughter, Rebecca Metzger, and upon the youngest of said children attaining the age of majority, all the then surviving children of my said daughter, Rebecca Metzger, shall be immediately entitled to said two thousand four hundred and ninety (2,490) shares in equal proportions.

Henriette Lachman."

The requirements of the deed were performed upon the contingencies occurring for which it provided.

On November 14, 1916, Henriette S. Lachman died, being then a resident of Alameda County, California, leaving an estate of the value of $302,963.64, which included 2,490 shares of the stock that passed to her upon the death of her husband and 25 shares of stock in a business that had been conducted by her husband but did not include the transfer of the 4,985 shares included in the trust deed.

The will was duly probated and the tax under the Act of September 8, 1916, was paid on the property which passed under her will, but no tax was paid on the 4,985 shares transferred 15 years before by the trust deed.

The Commissioner having ruled that those shares were subject to a tax, assessed against them the sum of $4,545.50. It was paid under protest and this action was brought for its recovery.

Wardell demurred to the complaint on the ground that it did not state facts sufficient to constitute a cause of action against him. The demurrer was sustained and judgment entered dismissing the complaint.

Stating the contention of the plaintiffs, the court said it was that "the act should not be construed as to include transfers made prior to its passage, and that if it be so construed the act is unconstitutional." The court observed that "both of these questions were determined adversely to the plaintiffs by the Circuit Court of Appeals for the Eighth Circuit in *Schwab, Executor* v. *Doyle*, not yet reported." And said further, "In that case the transfer was made in contemplation of death, whereas in the present case the transfer was intended to take effect in possession or enjoyment at or after death, but manifestly the same rule of construction will apply to both provisions, and the same rule of constitutional validity."

The court, while apparently relying on *Shwab* v. *Doyle*, declared that it entertained "no doubt that the act was intended to operate retrospectively, and a contrary construction could only be justified on the principle that such a construction would render the act unconstitutional."

The same contentions are made against and for the ruling of the court as were made in *Shwab* v. *Doyle*. It is not necessary to repeat them. They are, with but verbal variations, the same as in *Shwab* v. *Doyle* and the Commissioner so considering, submits this case upon his brief in that.

We have there stated them and passed judgment upon that which we think determines the case, that is, the retroactivity of the Act of September 8, 1916. The facts in this case fortify the reasoning in that. In this case the Act is given operation against an instrument executed 15 years before the passage of the Act.

The record exhibits proceedings that should be noticed. The demurrer of Wardell was sustained to the complaint, and a judgment of dismissal entered January 13, 1921.

On February 2, 1921, plaintiffs gave notice of a motion to substitute John S. Flynn as defendant in the place and stead of

Wardell in so far as the action was against Wardell in his official capacity, and to permit it to be continued and prosecuted against him so far as it was against him personally.

The grounds of the motion were stated to be that he had resigned and Flynn had been appointed his successor and was then the acting Collector.

On February 7, 1921, the motion was granted. The order of the court recited the resignation of Wardell and the succession of Flynn. And it being uncertain as to whether this was a proper case for the substitution of Flynn or was one which should proceed against Wardell, and it appearing to the court on motion of plaintiffs that it was necessary for the survivor to obtain a settlement of the questions involved, it was ordered that so far as the action was against Wardell in his official capacity, it might be sustained against Flynn as his successor, and that so far as it was against Wardell personally, it should be continued against him. And it was ordered that the action should thereafter proceed against Flynn and Wardell without further pleadings or process.

On February 9, 1921, Flynn filed an appearance by attorneys which recited that he had been substituted in the place of Wardell in so far as the action was against Wardell in his official capacity, and thereby appeared in the action as such defendant.

It will be observed that there was no resistance to the motion of substitution of Flynn nor exception by him, and that he almost immediately appeared in the action in compliance with the order of the court. The subsequent proceedings were directed as much against him as against Wardell, the bond upon the writ of error running to both.

However, this Court decided in *Smietanka, Collector* v. *Indiana Steel Company*, October 24th of this term, that a suit may not be brought against a Collector of Internal Revenue for the recovery of a tax, in the collection and disbursement of which, such officer had no agency. We think the bringing of Flynn into the case was error. Therefore, upon the return of the case to the District Court, he shall be permitted to set up the defense of non-liability, if he be so advised, and, if he set up the defense, it shall be ruled as sufficient for the reasons we have given.

Judgment reversed and cause remanded for further proceedings in accordance with this opinion.

suppose it would be, and the Supreme Court, in language already quoted, has held that the courts will not assume that Congress intended any such consequences. Union Pacific R. R. Co. vs. Snow, supra."

CONCLUSION.

It is respectfully submitted that the Act of 1916 should not be construed as taxing a decedent's estate in respect of transfers made before the passage of the statute, and that the judgment of the lower Court construing it retroactively should be reversed.

Respectfully submitted,

J. WALLACE BRYAN,

CHARLES McH. HOWARD,

AMICI CURIAE.

Washington, April 10, 1922.

APPENDIX.

UNITED STATES DISTRICT COURT.

DISTRICT OF MARYLAND.

No. 1109—AT LAW.

Filed November 29, 1921.

JOHN J. CURLEY ET AL.

VS.

GALEN L. TAIT ET AL.

J. Wallace Bryan, Charles McHenry Howard and *Joseph C. France* for the plaintiffs.

Robert R. Carman for the defendants.

ROSE, D. J.—

The plaintiffs, as executors of the executrix of the late William H. Grafflin, who died July 7, 1917, are here seeking to recover $23,927.22 paid the defendant under protest as an estate tax upon $285,655, being the aggregate value, at the testator's death, of various securities transferred at different times, within seven and a half years before he died, to either the Johns Hopkins Hospital or the Johns Hopkins University. As neither institution was, in the view of the Government, to get any substantial benefit from the property until after the tes-

tator's death; the defendant says that the transfers were not intended to take effect in enjoyment until that time and that in consequence, the tax was properly collected.

The facts said to make the other securities taxable did not exist as to some Russian Roubles Internal 5s, worth, at the testator's death, $2,255. The inclusion by the Government of these in its tax charge appears to have been the result of some mistake or misunderstanding. They were given by Grafflin outright, and as neither they nor any of the other property involved in this litigation was transferred in contemplation of death, the demurrer, so far as concerns the sum exacted upon them, must necessarily be overruled.

There are various minor differences in the terms of the transfers, but they were all alike in that by each of them, an out and out gift of the securities was made, and consummated by the issue and delivery of new certificates in the name of the grantee. It was expressly declared that the property conveyed was not charged with any trust. On the other hand, the hospital, or the university, as the case might be, covenanted in each of three agreements of transfer, that it would pay the net income during Grafflin's life to him, and after his death, and during such time as his wife should survive him, to her. After both of them were gone, the income, as well as the principal, was to be applied to the use of the grantee. The remaining one of the four, as it happened the earliest of them all in point of time, was in the nature of a marriage settlement. It recited that Grafflin was about to be married, and the hospital, with whom this particular agreement was made, covenanted to pay after the marriage was solemnized, the net income to the wife during her life, and afterwards to him during his life if he should prove to be the survivor.

APPENDIX (*Continued*).

By the terms of one of the agreements, the grantee, during the continuance of the life estate, was, after paying taxes, to retain 1 per cent. of the income for itself; by another 2½ per cent.; and by the others 5 per cent., but in that case it was itself to pay the taxes, whether they amounted to more or less than the 5 per cent. retained.

By most of them it was provided that anything in the nature of stock or bond dividends or payments on account of cumulative preferred dividends then in arrear, should be treated as additions to principal. To the man in the street, the enjoyment of a share of stock would be found in the right to apply to his own uses the dividends that might be declared upon it, and from this standpoint there is so much force in the Government's contention that neither hospital nor university enjoyed their gifts during Grafflin's lifetime, that without further discussion, it may, for the purpose of this case, be assumed to be sound, although it will be unnecessary so to decide. Even so, and upon the further assumption to be hereafter critically examined, that the statute is retroactive covers these transactions entered into years before it was enacted, the query remains, was the defendant justified in requiring the payment of the tax upon the full value of the stock transferred in contemplation of Grafflin's marriage, to the hospital, which covenanted to pay the net income thereof to the prospective wife during her life. Grafflin reserving nothing of substance to himself except the right to the net dividends during so much of his life as should extend beyond hers, thus making his interest dependent altogether upon the contingency that he should prove to be the survivor? The Government answers yes. It says that the hospital

was not to enjoy the stock until after his death. True, but is that all that is necessary?

If all beneficial ownership and possession irrevocably passes from the transferror at the time of the transfer, it would seem to be immaterial whether it goes to one person or to several, and if to several, whether their enjoyment is to be simultaneous or successive, and if the latter, at what time or upon the happening of what event the rights of one give place to those of another. In the instant case, had the agreement provided that after Mrs. Grafflin's death and during any period he survived her, the income should be paid to some one other than himself, there could, I imagine, have been no claim that any estate tax was chargeable. It follows that all that is taxable, if anything, is, in the language of the statute, "the interest" which he retained for himself. At the time the transfer was made, it was uncertain whether it would turn out to be worth much, little or nothing. As he died before his wife, it proved to be a fact valueless. If its taxable worth is to be ascertained as of the date of his death, as is the clear statutory rule when applicable, there is nothing to tax. Of course, at the time the agreement was made, the retained interest had an ascertainable value to those concerns which deal in insurance policies, annuities and like interests, the worth of any one of which is altogether uncertain, but the aggregate value of any large number of which can, from the mortality tables, be determined with approximate exactness.

The question of how much a contingent interest as Grafflin retained for himself under this agreement should be valued for estate tax purposes is not at all clear.

Apparently what the statute had in mind in declaring that the value of the gross estate of the decedent shall be determined by including the value at the time of his death, of all property, etc., is what it said. and no more. That is to say, the value of the property is to be then determined as of that date and not his interest in it, for if the latter were the case, any property which had been transferred by him in such manner that his interest ceased at death, would have no taxable value, and that is clearly that the statute does not mean.

At the hearing the Government was so confident that it was entitled to tax the full value of his interest and the plaintiffs so certain that none of it should be taxed, that neither of them discussed the question now mooted. As from what has been said it follows that the entire interest was not taxable, the demurrer to so much of the plaintiff's declaration as seeks to recover the tax exacted on all of it, must be overruled. The question of whether the Government was entitled to any part of the tax less than the whole need not be passed upon and should not be until the Court is enlightened by further argument.

All the above will be unimportant if the conclusion to which I have arrived upon another contention of the plaintiffs shall ultimately be sustained. They say that no tax at all was collectable, because the transfers here in controversy were all made before the statute was enacted. To this the Government has two answers. It says that the statute itself declares that it has reference to a transfer made "at any time." These words, however, are susceptible of a reasonable construction which could limit them to transactions taking place thereafter.

Congress may well have thought it important to make clear that the length of time before the death at which a transfer took place was not to be a controlling circumstance. The words used were apt to express that intention, and may well have been employed with the limitation usually implied that they were not to affect transactions which had already taken place. The rule, of course, is that statutes are not to be given a retroactive construction when by doing so, "antecedent rights are affected or human conduct given a consequence it did not intend." Union Pacific Railroad Company vs. Snow, 231 U. S. 204-213.

For reasons which will be hereinafter set forth, this statute, if retroactively applied, will, in some instances, cause serious hardship and injustice. The courts have gone to great lengths in construing away language which in its more natural import, seems to indicate that the Legislature intended the act should affect transactions which had been entered into before its passage. Union Pacific R. R. Co. vs. Laramie Stock Yards Co., 231 U. S. 190. If this were a case of first impression, I personally would have no hesitation whatever in holding that the Act of 1916 does not affect transfers made before it was passed.

But the Government says in the second place, that in Shwab vs. Doyle, 269 Fed. 321, the Circuit Court of Appeals for the Sixth Circuit held the act to be retroactive. Diversity of decision is especially unfortunate in the construction of tax statutes in which uniformity of interpretation and application are so important. Moreover, a court of equal rank would hesitate long before differing with a tribunal so eminent for wisdom and learning as that which has spoken on the subject. Nothing short of

the clearest conviction will justify a district judge in doing so, but there are rare occasions in which he must, because as the law does not make a decision of a Circuit Court of Appeals binding outside of its own circuit, the responsibility of determination is one from which he cannot escape.

In Shwab vs. Doyle, supra, the case of Wright vs. Blakeslee, 101 U. S. 174, was cited as authority for holding a similar statute retroactive. The act there construed imposed a tax upon the succession; that is, upon the right to receive, and was levied upon what passed to the heir, devisee, legatee, distributee or successor, and not upon the estate. Knowlton vs. Moore, 178 U. S. 41, 24 et seq. The distinction is neither pedantic nor technical, but as applied to the matter now in hand, is in the highest degree practical.

In Shwab vs. Doyle, supra, it was held that the addition made by the Act of 1918 (40 Stat. 1097), of the words "whether such transfer is made or occurred before or after the passage of the act," was a legislative construction rather than an amendment of the statute now under consideration. The Supreme Court has since taken the opposite view, as to other broadening language then first introduced. U. S. vs. Field, 255 U. S.

The case before the Circuit Court of Appeals was one of a transfer made in contemplation of death. It answered the objection to the practical hardships which a retroactive construction might entail by saying, "It is true that if the tax before us is retroactive, it might, at least theoretically, affect conveyances made many years before a grantor's death, but this consideration is hardly practi-

cal. Congress would, we think, scarcely be impressed with a practical likelihood that a transfer made many years before a grantor's death, say twenty-five years, to use plaintiff's suggestion, would be judicially found to be made in contemplation of death under the legal definition applicable thereof, and without the aid of the two years prima facie provision."

Apparently, the Court's attention was not drawn to some of the consequences which in a case like the one at bar, would follow from a retroactive construction. The present act, unlike its Federal predecessor, is an estate tax and not a tax upon the right to receive. If the Government's contention be sustained, the tax will come, not as in Wright vs. Blakeslee, supra, or in Cahen vs. Brewster, 203 U. S. 543, out of the sum received by the one to whom the taxed property passes, but will be collected from one to whom it does not. Neither the Johns Hopkins Hospital nor the Johns Hopkins University will pay one cent of it. It will all come out of property going to Grafflin's widow. Would Grafflin have made any of these transfers had he understood by so doing he would impose a charge upon his wife of upwards of $23,000? The care with which certain limitations were introduced into each of the agreements would seem to make it highly improbable. It is easy to conceive of a case in which a man of large estate might, before the passage of the Act of 1916, have made considerable transfers to relatives, friends or to charitable or educational institutions in somewhat the same fashion as Grafflin did, reserving for some residuary legatee, a comfortable and even handsome balance of his estate. If the Government is right, such legatee might be stripped of every penny of the testator's bounty. The taxes on the transferred property might amount to more

than the residue of the estate, large as the testator had every reason to suppose it would be, and the Supreme Court, in language already quoted, has held that the courts will not assume that Congress intended any such consequences. Union Pacific R. R. Co. vs. Snow, supra.

It follows that the demurrer to the declaration must be overruled generally.